Final

IN THE TRIBUNAL OF THE PENSION FUNDS ADJUDICATOR

CASE NO: PFA/EC/733/2003/NVC

In the complaint between:

L Botha **Complainant**

and

Central Retirement Annuity Fund **First Respondent**

Sanlam Life Insurance Limited **Second Respondent**

DETERMINATION IN TERMS OF SECTION 30M OF THE PENSION FUNDS ACT OF 1956

Introduction

[1] This is yet another retirement annuity fund case in a series of cases that demonstrate utter disregard by some life assurers for members' interests and compliance with the rules of the fund. What makes this case stand out is the extraordinary refrain by Sanlam that seems to suggest that "industry practice" trumps the law. And what makes this refrain even more extraordinary is the temerity even to make such a submission in light of Supreme Court of Appeal's rejection (as long ago as June 2001) of a similar argument as "breathtaking" and "cynical".

The facts

[2] The complainant commenced contributing to the fund in its Equity Focus Section with effect from 1 June 1998 (policy number: 17013915x8) and in its Offshore Equity Section (policy number 17117501x1) with effect from 1 September 1998 at the following rates:

Equity Focus Fund: Policy Number: 17013915x8

1/6/1998 to 31/1/1999 @ R 1 030 x 8 = R 8 240

1/2/1999 to 31/5/1999 @ R 2 061 x 4 = R 8 244

1/6/1999 to 30/9/1999 @ R 2 200 x 4 = R 8 800

1/10/1999 to 31/5/2000 @ R 255 x 8 = R 2 040

1/6/2000 to 31/5/2001 @ R 280 x 12 = R 3 360

1/6/2001 to 31/7/2001 @ R 302 x 2 = R 604

Total **R31 288**

Equity Offshore Fund: Policy Number: 17117501x1

1/9/1998 to 30/9/1999 @ R 1 030 x13 = R 13 390

1/10/1999 to 30/9/2000 @ R 255 x 12 = R 3 060

1/10/2000 to 31/5/2001 @ R 280 x 8 = R 2 240

1/6/2001 to 31/7/2001 @ R 302 x 2 = R 604

Total **R 19 294**

[3] On 18 July 2001 she requested Sanlam, the fund administrator and underwriter, to make both portfolios paid-up with immediate effect. In the same letter she requested Sanlam to confirm that no monies already paid in would be lost.

[4] In a letter dated 31 July 2001 from the "Front Office" Manager of Sanlam Life Division, she was advised that the offshore equity portfolio was made paid up. The letter continues to elaborate on the costs incurred, naming such costs as "marketing", "issuing" and "administration" costs. It also states:

> "Making your policy fully paid-up will result in our not receiving the charges we expected and the rest of the outstanding expenses will be deducted from the value of the policy."

[5] She was further advised by Sanlam Life Client Contact Centre, in a letter dated 11 March 2002, that the equity focus portfolio had been cancelled with effect from 1 August 2001 as "it did not have sufficient value to be made fully paid-up".

[6] In November 2003 the complainant requested Sanlam to reinstate the offshore equity fund. She subsequently received a letter dated 14 January 2004 from Sanlam (written in bold headline-type lettering: "**Policy is now void**") advising that that fund had been made paid-up in August 2001 and that its status was void. The letter also states:

> "The policy does not (and never will) offer any early retirement value, claims value or maturity value.
>
> As a result, we cancelled the policy and it is now void."

[7] The complainant is aggrieved that these funds (the equity focus fund and the offshore equity fund in which her contributions were supposed to be invested) are now said to be void and have no value whereas she had made contributions of R19 294 and R31 288 respectively, totalling R50 582.

[8] Sanlam's response in a letter dated 7 March 2005 is that:

> "Policy 17013915x8 [the equity focus portfolio] illustrated that should we be able to maintain a return of 12% we did not expect the policy to have a fund value prior to 1 June 2005. In contrast with this policy 17117501x1 [the offshore equity portfolio] illustrated that the policy would have a fund value of R887.00 on 1 September 2001 provided that we maintain a return of 12%."

[9] Sanlam further avers that they were unable "*owing to deteriorating economic conditions*" to provide a return of 12% on either of the investment funds prior to the complainant's request to make these funds paid-up (on 18 July 2001). It is not clear what the nature of these "*deteriorating economic conditions*" was.

[10] Clause 8 of both funds' documents (so-called policy documents) deals with "paid-up policy" and read as follows:

> "If a premium is not paid within the period of grace and the waiting period as indicated in the Schedule has not yet expired, the policy offers no further benefits. If the waiting period has already expired, the policy is converted into a paid-up policy with reduced benefits according to the practice of Sanlam."

(Where premiums are payable on a monthly basis, as in this case, the period of grace is 15 days in terms of clause 7 of both funds' "policy documents").

[11] When the complainant's funds were invested in the two portfolios in June 1998 and September 1998, respectively, the waiting period for a paid-up status for the equity focus portfolio was 25 months and for the offshore equity portfolio 24 months. These waiting periods are subject to change when the premium is adjusted by the member or when the assurer's expectations, such as investment yield and total premiums receivable, in respect of a particular portfolio, are not met.

[12] At some stage, Sanlam reduced the waiting period for the equity focus portfolio from 25 to 16 months (effective date not expressed) and in the case of the offshore equity portfolio from 24 to 13 months. In both instances, Sanlam says the waiting periods had expired owing to non-payment of contributions up to the complainant's request for reinstatement in November 2003. Thus, it is argued, the funds had to convert to paid-up status as set out in clause 8, with "reduced

benefits according to the practice of Sanlam", upon the expiry of the respective waiting periods.

[13] "Reduced benefits" is not defined in the "policy documents", nor is there any elaboration on what constitutes "practice of Sanlam". Ms T Fenthum, Sanlam's Client Relations consultant, further states in her letter of 7 March 2005 addressed to the Deputy-Adjudicator:

> "**Having a policy paid up**
>
> As you are most probably aware the costs in respect of issuing and maintaining a policy are recoverable by means of fees which are recovered from the premiums received over the term of the policy. Should a request be received to discontinue premium payments (i. e. having the policy made paid up), we will no longer be able to recover outstanding costs from the premiums. Consequently we recover the outstanding costs from the fund value of the policy."

[14] She adds in the same letter:

> "Costs incurred by Sanlam with regard to this policy are deducted in the normal course of business. The same applies with regard to outstanding costs that become accelerated in the event of the policy being terminated. The detail thereof is not embodied in the policy document. It has been the longstanding practice in the industry that certain material (notably the underlying actuarial and investment rules), are left to be incorporated in or adjuncted to the issued policy documents, by reference or necessary implication. Without this ancillary material the policy cannot be comprehended in full, and cannot be efficacious in the ordinary

business sense. Suffice to say, though, that it is accepted business practice for outstanding costs to be accelerated in the event of a policy being made paid up."

[15] The "policy document" under the heading "Investment Account" makes provision "*where applicable*" for "*policy fee and the costs of cover, rider benefits and administration*". It is nowhere indicated in what instances such costs would be inapplicable.

[16] Upon a request from this office to be provided with a breakdown of the fees outlined above, Sanlam provided schedules for both portfolios on 17 March 2005. Fees in respect of the equity focus portfolio from 1 June 1998 to 1 June 2001 are given as follows:

Policy fee	Administrative charge
R 437.95	R 1 609.36

[17] In respect of the offshore equity portfolio from 1 September 1998 to 1 August 2001, the fees are given as follows:

Policy fee	Administrative charge
R 279.30	R 907.46

[18] These schedules inform that the investment amount is equal to the annual premiums less the “policy fees” and “administrative charge” (there appears to be no cost of rider benefits).

[19] The “policy document” further states that the determination of the benefit is subject to investment growth. In fact it states, under “Provisos and Assumptions”:

> “The actual benefits afforded by this policy shall be determined by the actual growth rates, cost recoveries and bases of calculation applicable from time to time.”

[20] The rules of the fund refer to the paid-up status of a portfolio in rule 2 of part 7 and state:

> “2. A MEMBER’S CONTRIBUTIONS are payable during the period determined in the POLICY issued on his life.
>
> If a MEMBER'S CONTRIBUTIONS cease after he has already paid sufficient CONTRIBUTIONS so that the POLICY issued on his life has a paid-up value in accordance with the practice of the ASSURER, the ASSURER converts the POLICY to a paid-up POLICY for reduced benefits. The MEMBER will then have the right to apply for reinstatement of his benefits, partially or in full, and the MANAGEMENT COMMITTEE in consultation with the ASSURER, will consider such a proposal on receipt of:

2.1 all arrear CONTRIBUTIONS together with interest at such a rate as determined by the ASSURER from time to time; and

2.2 satisfactory proof of assurability where the ASSURER requires such proof."

Determination and reasons therefor

[21] Much of the language used by Sanlam in its responses is rooted in the misapprehension, with respect, that we are here dealing with a life policy. This tribunal has held on a previous occasion that a retirement annuity fund (such as the one here in issue) is not a life policy but a pension fund organisation as defined in the Pension Funds Act, 24 of 1956 (see *De Beer v Central Retirement Annuity Fund, PFA case number PFA/KZN/1357/2002/KM, 15 March 2005*, at paragraphs [3] – [7]). In the result, use of language in this context that is best suited to insurance policies is, with respect, misleading and gives rise to all sorts of consequences foreign to the workings of ordinary pension fund organisations. While mindful of the fact that this is an underwritten fund, the first respondent is nevertheless not thereby exempted from the provisions of section 13 of the Act. If Sanlam, as underwriter, is desirous of levying fees and other charges not provided for in the rules, it must first approach the trustees of the fund with a view to making application to the registrar for amendment of the rules to provide for such fees and charges (see part 10 rule 4). It cannot simply go ahead and levy such fees and charges on the strength of some "industry practice".

[22] Because we are here concerned with a pension fund organisation as defined, the provisions of section 13 of the Pension Funds Act apply. Consequentially, and as the Supreme Court of Appeal has pronounced on at least two occasions, the rules of this retirement annuity fund are King (see *Tek Corporation Provident Fund and Others v Lorentz [2000] 3 BPLR 227 (SCA) at paragraph [28]; Mostert NO v Old Mutual Life Assurance Company (SA) Ltd [2001] 8 BPLR 2307 (SCA) at paragraph [30]*). Nothing not provided for therein can properly be done.

[23] Now, there is no disclosure in the rules on the charging of costs. The rules and the "policy documents" are also silent on the charging of estimated future costs that the "policy" may endure if there is premature ceasing of premiums. There is also no allowance for the payment of a penalty in such circumstances, nor for the recoupment of costs after the "policy" becomes "paid-up", nor for the acceleration of the payment of such costs upon non-payment of premiums. The "policies'" reference to "reduced benefits" in accordance with the "practice of Sanlam" when a "policy" becomes "paid-up", and the benefits subjectivity to "cost recoveries" and the "calculation applicable from time to time", render the already extraordinary discretionary powers to Sanlam too intangible and open-ended to the obvious detriment of the member.

[24] Ms Fenthum's seemingly unperturbed refrain that "*the detail* [of costs] *is not embodied in the policy document …* [but that] *it has been the longstanding*

practice in the industry that [such detail] *be incorporated in or adjuncted* (sic) *to the issued policy documents … by necessary implication*" is, with respect, extraordinary. This kind of argument was rejected (and rightly so, with respect) by the Supreme Court of Appeal as "cynical" (see *Mostert NO v Old Mutual Life Assurance Company (SA) Ltd* [2001] 8 BPLR 2307 (SCA) at paragraphs [69] – [72]). In fact, that such a submission should even be made is breathtaking in its audacity and demonstrates utter disregard for transparency and the interests of retirement annuity fund members.

[25] The rules of the fund also only allude to "reduced benefits" in terms of the "assurer's practice" in the case of a "paid-up policy" without any specification, limitation or definition (see paragraph [20] above).

[26] What the trustees of a pension fund organisation may or may not do is decreed by the fund rules. Consequent upon the vagueness of both "policy documents" in relation to the equity focus portfolio and the offshore equity portfolio, respectively, on the one hand, and the rules as regards the recovery of costs, the calculation of a paid-up benefit, and what constitutes "practice" or "reduced benefits", on the other, I can find no legal basis for Sanlam's submission that the two portfolios have no value because of some unquantified costs that are not clearly set out in the rules. The only provision made in the "policy documents" is for the recovery of "policy fees" and "administration charges".

[27] In the result, I make the following order:

The first respondent is ordered to credit the complainant's investment accounts in the two portfolios in which her contributions or premium were invested, within four weeks of the date of this determination, with the total contributions made by her (totalling R50 582), less the quantified "policy fees" and "administration charges", as outlined in paragraphs [16] and [17] above (totalling R2 047,31 in respect of the equity focus portfolio and R1 186,76 in respect of the offshore equity portfolio), for the respective periods that she made contributions invested in the two portfolios, adjusted by the rate of interest achieved from the date of inception of such investments as follows:

- The equity focus portfolio in respect of contributions or premiums made from 1 June 1998 to 31 July 2001, and
- The offshore equity portfolio in respect of contributions or premiums made from 1 September 1998 to 31 July 2001.

DATED at Cape Town this 22nd day of March 2005.

Vuyani Ngalwana

Pension Funds Adjudicator

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Section 30M filing: Magistrate's Court